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SUBJECT: PLANNED MEGAPORT IN BAJA CALIFORNIA COULD RELIEVE CONGESTION AT U.S. PACIFIC PORTS

REF: Mexico 949

SUMMARY: Construction of the long-planned and continually delayed Punta Colonet port, 150 miles south of San Diego, CA, is a top priority for the state government of Baja California. Optimistically, the state and federal governments hope developers will begin construction in 2009, and that the port will start partial operations three years later. The port would be another Baja California link to Asia, but the main purpose is to relieve saturation at the Los Angeles and Long Beach ports, as most of the port's goods from Asia will be destined for the U.S. Several legal and coordination problems have slowed down the bidding process, and it is not yet clear if the project will leave the drawing board.

PLANS FOR A NEW PORT

¶12. Since 2004, the Mexican federal government has been trying to implement the construction of a new port in Punta Colonet, Baja California. Since then, the project has experienced the impacts of government transitions and conflicts with other economic projects in the area. The construction will require an investment of about USD 9 billion and, if constructed, would be the most important port in the Mexican Pacific, with an annual capacity of about 6 million TEU's (a container of twenty-foot equivalent units), with 90% of the imported containers going to the U.S. There are no other similar ports in the area; the Port of Ensenada, operated by Hutchison Port Holdings, in 2007 managed only 127 thousand TEUs.

¶13. The increasing international trade between North America and Asia and the overcrowding of the two main ports on the American west coast, Long Beach and Los Angeles, motivated plans for the new port. With China alone, from 2005 to 2006, U.S. trade increased over 16%. Neither Long Beach nor Los Angeles can satisfy the increased shipping capacity of the new generation of cargo ships. From 1998 to 2002 the cargo operated by these ports grew from 6.9 million TEUs to 9.9 million. In 2007, both ports processed about 15 million TEUs.

¶14. If it becomes a reality, the Punta Colonet Port will be established in a sparsely populated area of twenty square kilometers and would become fully operational within ten years of beginning construction. The GOM envisions that the port will consist of an airport, a railway to the U.S., and ten docks, connected with the rest of the state with new federal roads. While the state government has sponsored some feasibility studies conducted by Mexican and transnational companies, neither the state nor federal government have specific plans and are leaving these tasks to the company or consortium that wins the contract. The winning company would construct and operate the different parts of the multimodal port, including the vital railway to connect it with the U.S. In addition, there will be a need for urban and industrial infrastructure. The Baja government projects that the population in the area could grow to 100,000 people after ten years of the port's operations.

PROBLEMS IN THE PROJECT

¶15. The bidding process to construct the port has been stuck for several years. Since coming to office in August 2007, the PAN administration of Governor Osuna Millan has made pushing

forward the Punta Colonet project a priority. It created an office to coordinate the project activities between federal government officials and local authorities, presided by Josi Rubio Soto. According to Mr. Rubio, the lack of coordination between government agencies explains the delays in the call for bids.

¶16. For example, as a result of this lack of coordination, the federal government is involved in a legal controversy with a Mexican mining company for land usage in Punta Colonet. The Federal Secretary for Economy (SE) granted a concession to Grupo Minero Lobos (GML) in August 2005 to mine titanium and magnetite in the coast waters near Punta Colonet, even though the area already had been identified for the port project by the Secretary for Communications and Transports (SCT). In order to continue with plans for the port, the federal government tried to pull back the concession, causing GML to file a lawsuit.

¶17. Further complicating the picture, GML had formed an alliance with the American company Stevedoring Services of America (SSA), which already operates several port locations in Mexico. The two companies wanted a part in the construction of the port at Punta Colonet, and after the government pulled its concession to GML, both tried to negotiate a deal to construct and operate one of the docks at Punta Colonet without participating in an open bidding process. When that didn't pan out, SSA decided to leave the alliance; analyst say given its interest in Mexican ports, SSA wanted to remain on good terms with the government.

¶18. With the change of the state government in Baja California in 2007, the negotiations with GML appear to have eased. According to Mr. Rubio, the state and federal governments have reached an agreement with GML, so that mining and port projects can coexist. Company representatives have declared they are willing to withdraw their lawsuits from the courts, though this has not yet happened.

¶19. Even if the GML imbroglio is resolved, it is unclear when the federal government will move forward with a call for bids. Mr. Rubio said the bidding process could be launched at the end of July to begin construction in 2009. At the same time, some federal officials have declared the call for bids will be held later in 2008. Alejandro Chacsn, the Ports and Merchant Marine General Coordinator from the SCT said the government would call for bids at the end of 2008, and Alejandro Delgado Oscoy, a federal deputy who chairs the Commission for Transports in the Chamber of Deputies, told press there is no certainty about the date to launch the bidding process, but that it may be published at the end of this year.

CORPORATE INTERESTS

¶10. Some companies have formed strategic alliances around the opportunity of this mega project. Mexican companies Grupo Carso and Ferromex have declared they would participate in a joint venture. The well known former Baja California Governor, Ernesto Ruffo Appel, leads a group of shipping companies in the conglomerate "Puerto Colonet Infraestructura", which has acquired several land properties in the area and has lobbied in favor of the project. Hutchison Port Holdings may participate, as it has experience operating Baja's current most important port, Ensenada, as well as the American Marine Terminal Corporation.

¶11. However, the government's delays have caused some companies to give up. The American company Union Pacific, which had allied with Chinese Hutchinson Port Holdings declared in 2007 it would not participate in a future bidding team. The company had planned to construct the railway to connect the port with the United States through the Yuma Dessert, and had conducted several feasibility studies.

¶12. COMMENT: If it becomes a reality, Punta Colonet will increase Baja's economic integration with both Asia and the U.S. and make the state an even more important portion of many U.S. companies' supply chains. The project may have surpassed several of its most notable problems, such as the lack of

coordination between governmental agencies and the litigation with the Grupo Minero Lobos. At least so far, local landowners have not staged protests against the construction of the port and many of them are already in discussion with investors and the government to sell their plots. The port is a high priority for Governor Millan and is the top feature of his development plan for the State. Still, a lack of clarity in the bidding process and the failure of either the state or federal government to make detailed plans could yet hamper the project.

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